CLEVELAND PUBLIC LIBRARY
BUSINESS INF. BUR.
CORPORATION FILE

RJR Quarterly Report 2

TO STOCKHOLDERS OF R. J. REYNOLDS INDUSTRIES, INC. SECOND QUARTER 1977

RJR board elects three directors, one executive VP

Three new members have been elected to the RJR board of directors. One of the new directors has also been named as an executive vice president.

The newly elected directors are: William S. Anderson, chairman and chief executive officer of NCR Corp.; J. Dwayne Taylor, formerly a director and executive vice president of Sun Co., Inc.; and Michael R. McEvoy, R.J. Reynolds executive vice president. Taylor was also elected an RJR executive vice president, responsible for the Company's energy business.

William S. Anderson

Michael R. McEvoy

J. Dwayne Taylor

Anderson has had a long career with NCR, beginning as manager of NCR Hong Kong after serving in World War II. After directing NCR's operations in the Far East until 1972, he moved to world headquarters at Dayton, Ohio, as the company's president.

Taylor takes the place of J. B. Sunderland as executive vice president responsible for energy on RJR's management committee. Sunderland had previously asked to be relieved of his duties as executive vice president so that he could devote full time to the operations of Aminoil International, Inc., where he is president and chief executive officer.

Prior to joining RJR, Taylor most recently served as executive vice president of Sun Co., Inc. He joined Sun in 1951 as a geologist and became executive vice president and a member of the Sun board in 1973.

McEvoy was elected executive vice president in September 1976 when the management committee was created. He is responsible for the transportation sector of the Company's business. Before his election as executive vice president, McEvoy was chairman and chief executive officer of Sea-Land Service, Inc., the Company's containerized shipping business.

Real introduction off to good start

Real is advertised on the world's largest painted sign on New York's Times Square.

Real, RJR's new low "tar," all-natural cigarette brand, has gotten off to an extremely successful start for its nationwide introduction, which began June 13.

Both trade and consumer response to the new brand have been favorable, according to Charles A. Tucker, group vice

(Continued on page 2)

Earnings, sales up in 2nd quarter, 1st half

Net earnings of R.J. Reynolds Industries, Inc. increased 4.6 percent to $100 million or $1.94 a fully diluted share in the three months ended June 30, compared with a year earlier. Sales and revenues rose 22 percent to $1.67 billion.

First-half net earnings were up 9.9 percent to $188.1 million or $3.65 a fully diluted share. Sales and revenues rose 21 percent to $3.22 billion.

Financial report begins on page 4.

(Continued from page 1)

Real introduction

president and director of marketing.

"Although Real has not been on the market long enough for us to obtain definite consumer information, our preliminary reports look very good," Tucker says. "We expect to strengthen Real's consumer acceptance with our sampling and couponing programs. These are the most extensive programs of their kind to ever support any cigarette brand."

Trade distribution has been "excellent," Tucker notes.

"So far Real has met or exceeded every goal we'd established for shipment and trade distribution."

The brand has shown "outstanding performance" among bellwether retail accounts, Tucker adds.

"Before we introduced Real, we selected 300 grocery and drug store chains with 20 or more stores as key sales targets," he explains. "We felt these would give us an important indication of the brand's acceptance. So far, 298 of the 300 chains have purchased Real.

"In addition, we have already surpassed our goal of 250,000 vending commitments (columns of cigarettes in vending machines) by more than 50,000."

Aminoil wins six bids

Aminoil USA was successful in six of its bids for leases with potential for oil and gas development offshore Louisiana in the federal sale held June 23. Aminoil's share of the six leases ranges from 4.5 percent to 50 percent and cost a total of nearly $11 million.

Sea-Land to build four ships, crane

Sea-Land Service has contracted for a program that will create four new-technology vessels using the midbodies of the company's four T-3 containerships. Mitsubishi Heavy Industries will join four new power plants and four new bows to the T-3 midbodies. The project will result in the addition of four vessels with capacity of 590 containers each to the Sea-Land fleet next year.

Also, the company will build a second container crane at the terminal it operates at Portsmouth, Virginia. The new crane is expected to halve the time Sea-Land's SL-7 containerships spend in the port — from 24 hours to no more than 12. The 30-ton-capacity crane is scheduled for completion within a year at an estimated cost of $3 million.

Reynolds Tobacco sponsors fiesta

Winston, Puerto Rico's largest-selling cigarette, helped provide New York City's Puerto Rican population with a reminder of its homeland recently through sponsorship of the Fiesta de San Juan Bautista, New York's largest annual ethnic festival. The festival, honoring the partron saint of Puerto Rico, included religious services, music and dance presentations and other cultural exhibits. More than 350,000 people came to Central Park to participate in the event.

Camel inspires fashion in Germany

R.J. Reynolds Tobacco GmbH has successfully launched a promotion based on a Camel Way of Life theme. The campaign features celebrity Bob Beck and has created a fashion trend in Germany.

R.J. Reynolds Tobacco GmbH has successfully launched a promotion based on a Camel Way of Life theme. The campaign features celebrity Bob Beck and has created a new fashion trend in Germany. The Camel Collection of clothing in the promotion has a casual safari appearance and was designed as leisure wear appealing to the Camel target group (men, aged 18-40, urban, modern, progressive, middle-upper class). The Camel trademark is subtly prominent on all the clothing in the collection and every fashion has a complete Camel label on the inside. The collection is being sold primarily in medium-priced retail outlets, including department stores.

Aminoil installs new offshore rig

Aminoil Development, Inc. has installed an eight-pile 24-slot drilling and production platform on High Island Block A-317 in the Gulf of Mexico. The platform was set in 217 feet of water at an estimated cost of $7.4 million.

Development drilling from the platform is scheduled to start in August, with gas production expected in the latter half of 1979.

Aminoil is the operator for a 13-member group that acquired the lease in a June 1973 federal offshore lease sale for a gross bonus bid of $77.7 million. Aminoil paid $46.6 million for its 60 percent interest at that time.

Five exploratory wells drilled to date indicated economically recoverable reserves of natural gas.

Services expanded

Sea-Land Service, Inc. has doubled its containership service to the Middle East. Eight containerships are now deployed in the weekly U.S.-Mideast service.

Also, in mid-July the company initiated direct containership service between Baltimore, Charleston, Jacksonville, and San Juan, Puerto Rico.

Fruit Juicy-Red selling in soft drink outlets

Twelve-ounce cans of Fruit Juicy-Red Hawaiian Punch are now available through soft drink outlets in more than half the United States.

The soft drink program enables RJR Foods to place America's most popular noncarbonated fruit drink in outlets not available to fruit drinks — vending machines, restaurants and the soft drink section of supermarkets.

A total of 35 bottlers from coast to coast are selling Hawaiian Punch in 12-ounce cans, using their established distribution channels. In most cases, Hawaiian Punch has become the second or third best seller behind the bottlers' main product.

Sales in 1976 topped 100 million cans. Future plans call for national distribution and possibly the introduction of other Hawaiian Punch flavors.

Menthol 'A' Lights enters test markets

Macdonald Tobacco Inc. has launched Export 'A' Lights Menthol into two test markets in the Canadian provinces of Alberta and Quebec. The new product complements Export 'A' Lights regulars, which were successfully introduced into the Canadian market last year and are now an established brand nationwide.

Report from the Chairman and President

Colin Stokes

J. Paul Sticht

R.J. Reynolds Industries, Inc. recorded net earnings of $100 million in the three months ended June 30, up 4.6 percent from $95.6 million a year earlier. Fully diluted earnings per share increased to $1.94 from $1.87. Consolidated sales and revenues rose 22 percent to $1.67 billion, compared with $1.36 billion in the year-ago period.

Net earnings were up 9.9 percent to $188.1 million in the six-month period ended June 30, from $171.2 million a year earlier. Fully diluted earnings per share rose to $3.65 from $3.35. Sales and revenues increased 21 percent to $3.22 billion from $2.67 billion.

We are pleased the second quarter topped last year's results. The 1976 second quarter was exceptionally strong, and was the best quarter of the year.

Both the domestic and international tobacco businesses contributed in a major way to the second-quarter performance, and the investment Sea-Land has made in redeploying some of its vessels should enhance results in the second half of the year.

We had said earlier that we would be hard pressed to equal last year's second-quarter performance, but felt that our growth performance for the year would show a healthy improvement. We currently do not see anything in the third or fourth quarters that would prompt us to change our evaluation of total 1977 performance.

The increased second-quarter sales were the result of generally improved sales performance in most of the Corporation's businesses. About 43 percent of the sales increase came from domestic petroleum operations acquired in mid-1976 and not included in year-ago figures. The remainder of the sales increase was largely attributable to the domestic and international tobacco businesses, as well as contributions from transportation and international petroleum.

Earnings from operations (EFO) totaled $222.4 million, up 14 percent from the 1976 period. International tobacco, domestic tobacco and domestic petroleum were the principal contributors to the increase.

For the six-month period EFO increased 16 percent to $418.4 million. The domestic tobacco, international tobacco, domestic petroleum and transportation businesses were responsible for most of the increase.

Foreign currency translation, required under FASB-8, which gives rise to unrealized noncash exchange gains and losses, produced a negative swing of 4 cents per fully diluted share in the second quarter, compared with second quarter 1976; and resulted in a favorable swing of 12 cents per fully diluted share in the first half, compared with the like period in 1976.

Domestic Tobacco

Sales of R.J. Reynolds Tobacco Company increased 8 percent to $726.4 million for the three months ended June 30, and EFO was up 12 percent to $149.9 million. Unit sales increased during the period, partly because of substantial orders for the company's new brand, Real, which was introduced nationally on June 13. Vantage, the company's major low "tar" brand, showed an increase of more than 25 percent over the 1976 second quarter.

For the first half, sales rose 6.1 percent to $1.37 billion, and EFO increased 10 percent to $287.7 million. Increased unit sales and the carryover effect of last year's price increase more than offset cost increases for both the second quarter and first half.

International Tobacco

Second-quarter sales of R.J. Reynolds Tobacco International, Inc. increased 19 percent to $321.7 million, compared with second quarter 1976, while EFO more than doubled to $27.6 million. Included in the improved performance was a 15 percent increase in unit cigarette sales.

In the first half, sales increased 14 percent to $616.7 million, with about one-third of the increase coming from higher volumes. Unit sales increased 4 percent in the first half. EFO was up 70 percent to $45.2 million in the half.

Transportation

Revenues of Sea-Land Service, Inc. increased 13 percent in the second quarter to $237.3 million, while EFO slipped 1.5 percent to $34.7 million. For the first half, sales rose 14 percent to $456.5 million, while EFO was up 20 percent to $63.3 million.

Sales gains were attributable primarily to expanded services to the Middle East and a strong showing in the Pacific and Atlantic trades. In the second quarter, sales gains were more than offset by normal startup costs for new services to the Middle East, including a major redeployment of vessels from domestic to foreign services. Higher foreign operating costs, due to unfavorable dollar exchange rates, also affected second-quarter and first-half earnings. Higher revenues more than offset higher costs in the first half.

Domestic Petroleum

Sales in the domestic petroleum business in the second quarter totaled $134.4 million, resulting almost entirely from the Burmah Oil properties purchased at midyear 1976. EFO associated with the domestic energy business was $6.4 million. Included in EFO in the latest quarter is a $4 million recognition of recovery of contested ad valorem taxes relating to several prior years.

First-half domestic petroleum sales were $295.2 million, also attributable almost entirely to the Burmah properties. EFO was $12.3 million for the six-month period.

The negative EFO figures for the second quarter and first half of 1976 are primarily due to exploration expenses related to undeveloped domestic properties owned prior to the Burmah acquisition.

International Petroleum

Sales in the international petroleum business increased 33 percent to $150.4 million in the second quarter, while EFO fell to $3.5 million. For the first half, sales were up 13 percent to $273.7 million, while EFO declined to $5.3 million. The EFO declines were attributable to higher costs absorbed in the first and second quarters.

The company is currently engaged in discussions with the Kuwait government regarding financial arrangements under the company's concession agreement. These discussions are a continuation of negotiations begun in February 1976.

Foods and Beverages

Sales at RJR Foods of $73.3 million for the second quarter were about even with year-ago results. EFO declined to $3.6 million, primarily because of marketing costs to introduce new Hawaiian Punch Drink Mix flavors and generally higher marketing costs to support the company's Drink Mix business.

Sales in the first half increased 5.6 percent to $150.6 million, mainly becase of Hawaiian Punch Drink Mix. EFO declined to $11.1 million. The factors affecting first-half EFO were similar to those described for the second quarter.

Aluminum Products and Packaging

Sales at RJR Archer increased 16 percent in the three months ended June 30 to $44.6 million, and EFO rose 19 percent to $3.6 million. For the first half, sales rose 15 percent to $88.2 million and EFO gained 14 percent to $6.8 million. Increased prices and volumes accounted about equally for gains in both periods.

The company is continuing to pursue its previously announced intention to sell its consumer division and still anticipates that the sale will have little impact on 1977 performance.

Nonoperating Item

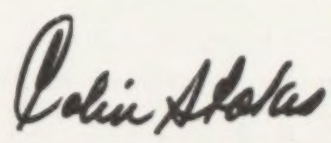
Interest and debt expense increased approximately $6.8 million in the second quarter and about $21.6 million in the first half of 1977, compared with year-ago periods. The increase was primarily attributable to interest expense on borrowings the Company obtained to finance the acquisition of the former Burmah Oil properties on June 30, 1976.

Dividends

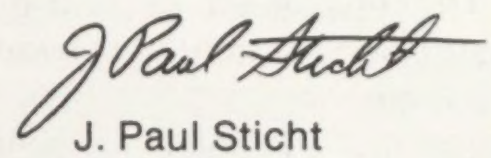
A dividend of 82 cents a share on the Common Stock was declared July 21, payable September 6 to shareholders of record August 10.

Financial Statements

The accompanying condensed financial statements are unaudited, but in management's opinion they contain all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of financial position as of June 30, 1977 and 1976, the changes in financial position for the six-month periods then ended, and the results of operations for the three-month and six-month periods then ended.



Colin Stokes
Chairman



J. Paul Sticht
President

August 15, 1977

R. J. REYNOLDS INDUSTRIES, INC.

CONSOLIDATED SUMMARY OF OPERATIONS

(Dollars in Thousands Except Per Share Statistics)

	Three Months Ended June 30		Six Months Ended June 30	
	1977	1976	**1977**	1976
Net sales and revenues (Note 2):				
Domestic tobacco	**$ 726,422**	$ 672,596	**$ 1,374,433**	$ 1,295,626
International tobacco	**321,698**	269,990	**616,730**	541,281
Transportation	**237,260**	209,761	**456,508**	400,534
Domestic petroleum	**134,392**	107	**295,177**	107
International petroleum	**150,352**	113,394	**273,729**	241,926
Foods and beverages	**73,302**	73,383	**150,624**	142,623
Aluminum products and packaging	**44,581**	38,377	**88,175**	76,852
Other (principally intercompany eliminations)	**(20,583)**	(14,069)	**(36,675)**	(29,879)
Consolidated	**$1,667,424**	$1,363,539	**$ 3,218,701**	$ 2,669,070
Earnings from operations (Note 3):				
Domestic tobacco	**$ 149,850**	$ 133,900	**$ 287,651**	$ 260,352
International tobacco	**27,563**	11,907	**45,163**	26,592
Transportation	**34,672**	35,215	**63,276**	52,831
Domestic petroleum	**6,448**	(2,263)	**12,307**	(4,540)
International petroleum	**3,478**	13,276	**5,277**	18,191
Foods and beverages	**3,563**	4,469	**11,139**	11,633
Aluminum products and packaging	**3,579**	3,020	**6,847**	5,984
Other (principally unallocated corporate expense)	**(6,715)**	(5,117)	**(13,284)**	(9,992)
Consolidated	**222,438**	194,407	**418,376**	361,051
Interest and debt expense	**(20,706)**	(13,914)	**(46,763)**	(25,165)
Other income (expense), net	**5,188**	3,839	**7,407**	6,858
	206,920	184,332	**379,020**	342,744
Foreign currency gains (losses):				
Realized	**(1,092)**	(1,060)	**(1,666)**	(1,459)
Unrealized	**(3,199)**	1,860	**2,000**	(4,480)
Earnings before provision for income taxes	**202,629**	185,132	**379,354**	336,805
Provision for income taxes (Note 4)	**102,591**	89,522	**191,254**	165,604
Net earnings	**100,038**	95,610	**188,100**	171,201
Less preferred dividends	**1,788**	2,597	**4,003**	5,258
Net earnings applicable to Common Stock	**$ 98,250**	$ 93,013	**$ 184,097**	$ 165,943
Net earnings per common share (Note 5):				
Primary	**$ 2.05**	$ 2.03	**$ 3.89**	$ 3.63
Fully diluted	**1.94**	1.87	**3.65**	3.35
Dividends per common share	**.82**	.77	**1.64**	1.54
Average number of common shares outstanding:				
Primary			**47,305,177**	45,709,005
Fully diluted			**51,577,323**	51,086,670

See Notes to Consolidated Condensed Financial Statements.

R.J. REYNOLDS INDUSTRIES, INC.

CONSOLIDATED CONDENSED BALANCE SHEETS

June 30

(Dollars in Thousands)

	1977	1976
ASSETS		
Current assets:		
Cash and short-term investments (Note 6)	**$ 124,969**	$ 119,062
Accounts and notes receivable, net	**591,818**	494,235
Inventories (Note 7)	**1,314,438**	1,254,815
Prepaid expenses	**27,247**	23,199
Total current assets	**2,058,472**	1,891,311
Property, plant and equipment - at cost	**2,924,183**	2,668,904
Less allowances for depreciation, depletion and amortization	**947,834**	745,921
Net property, plant and equipment	**1,976,349**	1,922,983
Cost in excess of net assets of businesses acquired	**170,042**	170,945
Other assets and deferred charges	**161,203**	157,569
	$4,366,066	$4,142,808
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable to banks (Notes 10 and 11)	**$ 58,298**	$ 656,495
Accounts payable and accrued accounts	**560,234**	473,124
Current maturities of long-term debt	**45,614**	63,726
Income taxes accrued	**145,147**	117,256
Total current liabilities	**809,293**	1,310,601
Long-term debt (less current maturities) (Notes 10 and 11)	**788,992**	546,887
Other noncurrent liabilities	**83,538**	79,117
Deferred revenue (Note 10)	**226,883**	9,010
Deferred income taxes	**215,354**	197,960
Stockholders' equity (Notes 8 and 11):		
Preferred Stock	**33,191**	48,631
Common Stock	**240,015**	229,060
Paid-in capital	**143,769**	107,150
Earnings retained	**1,825,031**	1,614,392
Total stockholders' equity	**2,242,006**	1,999,233
	$4,366,066	$4,142,808

See Notes to Consolidated Condensed Financial Statements.

R. J. REYNOLDS INDUSTRIES, INC.

CONSOLIDATED CONDENSED STATEMENTS OF CHANGES IN FINANCIAL POSITION

Six Months Ended June 30
(Dollars in Thousands)

	1977	1976
Working capital was provided by:		
Operations:		
Net earnings	**$188,100**	$ 171,201
Depreciation, depletion and amortization	**112,625**	65,499
Deferred income taxes	**21,539**	4,796
Long-term foreign currency translation (gains) losses	**807**	1,144
Other	**2,187**	4,097
Total from operations	**325,258**	246,737
Proceeds from long-term debt (Note 11)	**155,266**	4,410
Proceeds from issuance of Company's stock	**36,369**	8,405
Other (principally disposals of property, plant and equipment)	**10,730**	8,825
	527,623	268,377
Working capital was used for:		
Net increase in long-term assets from acquisition accounted for as a purchase (Note 10)	**—**	495,116
Capital expenditures	**146,890**	67,841
Cash dividends	**81,692**	75,634
Long-term debt becoming currently payable	**22,335**	16,531
Retirement of Preferred Stock upon conversion	**11,416**	2,615
Cost of treasury shares purchased	**1,639**	514
Reduction in deferred revenue (Note 10)	**36,438**	—
Other (principally other assets and deferred charges)	**6,380**	12,353
	306,790	670,604
Increase (decrease) in working capital	**$220,833**	$(402,227)

See Notes to Consolidated Condensed Financial Statements.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

Note 1
Accounting Change

During 1977 the Company changed its method of accounting for leases in conformity with the requirements of Statement No. 13 published by the Financial Accounting Standards Board in November 1976. All prior periods have been restated to reflect this change. The change had no material effect on assets, liabilities or net earnings.

Note 2
Excise Taxes

Net sales and revenues include excise taxes on tobacco and petroleum products as indicated in the following table:

(Dollars in Thousands)

	Three Months Ended June 30		Six Months Ended June 30	
	1977	1976	**1977**	1976
Domestic tobacco	**$220,829**	$217,051	**$418,041**	$417,418
International tobacco	**161,294**	148,879	**320,848**	288,211
Domestic petroleum	**3,743**	—	**6,975**	—
	$385,866	$365,930	**$745,864**	$705,629

Note 3
Costs and Expenses

For interim reporting purposes, certain costs and expenses are charged to operations in proportion to the estimated total annual amount expected to be incurred.

Note 4
Income Taxes

The provision for income taxes includes both amounts due currently and amounts that are deferred and that may be payable in future years. The provision for deferred income taxes amounted to $14,811,000 and $3,341,000 for the three months ended June 30, 1977 and 1976, respectively, and $21,539,000 and $4,796,000, respectively, for the six-month periods then ended.

Note 5
Earnings Per Share

Primary net earnings per common share are determined by dividing net earnings applicable to Common Stock by the average number of common shares and equivalent common shares outstanding.

Fully diluted earnings per common share are calculated using the "treasury stock" method. This method assumes that all shares of the Preferred Stock outstanding during the period were converted into Common Stock and the proceeds used to purchase treasury common shares at the higher of the average daily price or period-end closing price of the Common Stock.

Note 6
Cash and Short-term Investments

Short-term investments at June 30, 1977 and 1976, valued at cost (approximate market), amounted to $35,374,000 and $4,234,000, respectively.

Note 7
Inventories

The major classes of inventory and the amount of each at June 30 were:

	(Dollars in Thousands)	
	1977	1976
Leaf tobacco	**$ 940,873**	$ 912,860
Manufactured products	**114,093**	101,054
Excise tax on manufactured products removed from bond	**82,800**	74,453
Petroleum products	**26,998**	23,654
Other materials and supplies	**149,674**	142,794
	$1,314,438	$1,254,815

Note 8
Common and Preferred Stock

During the second quarter of 1977, 769,663 shares of the Company's $2.25 Convertible Preferred Stock (without par value), stated value of $10.57, were converted into 1,154,491 shares of Common Stock (par $5). Of the authorized but unissued common shares (60,000,000 shares authorized; 48,003,018 and 45,811,966 shares outstanding at June 30, 1977 and 1976, respectively) 4,710,231 shares were reserved for issuance upon conversion of 3,140,154 shares of $2.25 Convertible Preferred Stock (authorized 3,152,104 and 4,612,812 shares; outstanding 3,140,154 and 4,600,862 shares at June 30, 1977 and 1976, respectively).

Note 9
Contingent Matters

During the three months ended June 30, 1977, there have been no significant developments with respect to pending or threatened litigation, commitments or other contingencies (including those referred to in Note 8 to the Financial Statements in the Company's Annual Report for the fiscal year ended December 31, 1976, and Note 9 to the Consolidated Condensed Financial Statements in the Company's Quarterly Report for the quarter ended March 31, 1977) that, in management's opinion, would have a material effect on the Company's financial statements.

Note 10
Acquisition

On June 30, 1976, the Company acquired the outstanding capital stock of the principal U.S. subsidiaries of the Burmah Oil Company, Limited for approximately $522 million in cash. The consolidated operating results of the Company include the operations of the acquired companies from the date of acquisition.

The acquisition was financed initially by short-term borrowings, which have been subsequently replaced by the sale in September 1976 of a $280 million nonrecourse production payment (see Note 6 to the Financial Statements in the Company's Annual Report for the fiscal year ended December 31, 1976), $100 million in 8.9 percent long-term notes issued in October 1976, and by funds received as described in Note 11 to these Consolidated Condensed Financial Statements.

Note 11
Issuance of Long-term Debt and Secondary Offering of Common Stock

On April 13, 1977, the Company issued $150,000,000 principal amount of 8% Sinking Fund Debentures. On April 14, 1977, pursuant to a registered underwritten secondary offering, certain underwriters acquired from a stockholder of the Company 600,000 shares of Industries' $2.25 Convertible Preferred Stock. The Preferred Stock was converted by the underwriters into 900,000 shares of Industries' Common Stock which was offered to the public. Upon conversion, $13,200,000 was received from the underwriters.

Of the net proceeds received by Industries in respect to the foregoing, $140,000,000 was used for reduction of Notes Payable to Banks, with the balance being used for working capital and other corporate purposes.

Inquiries

Communications concerning transfer requirements and lost certificates should be directed to either Transfer Agent: The Chase Manhattan Bank, N.A., 1 New York Plaza, 14th Floor, New York, N.Y. 10015, or First Jersey National Bank, 2 Montgomery St., Jersey City, N.J. 07303

Communications concerning dividends and change of address should be directed to R.J. Reynolds Industries, Inc., Shareholder Services Dept., Box 2959, Winston-Salem, N.C. 27102.

Board of Directors

JOSEPH F. ABELY, JR.
WILLIAM S. ANDERSON
C. F. BENBOW
ALBERT L. BUTLER, JR.
HERSCHEL H. CUDD
GORDON GRAY
WM. D. HOBBS
WALTER L. LINGLE, JR.
JOHN D. MACOMBER
MICHAEL R. McEVOY
CHARLES F. MYERS, JR.
JAMES R. PETERSON
H. C. ROEMER
J. PAUL STICHT
COLIN STOKES
J. DWAYNE TAYLOR
J. TYLEE WILSON

Officers

COLIN STOKES
Chairman and Chief Executive Officer

J. PAUL STICHT
President and Chief Operating Officer

JOSEPH F. ABELY, JR.
Executive Vice President and
Chief Financial Officer

MICHAEL R. McEVOY
Executive Vice President

JAMES R. PETERSON
Executive Vice President

J. DWAYNE TAYLOR
Executive Vice President

J. TYLEE WILSON
Executive Vice President

C. F. BENBOW
Senior Vice President and Secretary

RODNEY E. AUSTIN
Vice President

DENNIS DURDEN
Vice President

E. C. RITCHELL
Vice President

H. C. ROEMER
Vice President and General Counsel

R. D. THOMPSON
Vice President

J. W. DOWDLE
Treasurer

J. A. HAGAN
Comptroller

RJR talks to securities analysts in N.Y., Richmond

Joseph F. Abely, Jr.

J. B. Sunderland

New York Meeting

Late last spring R.J. Reynolds Industries, Inc. and its operating companies made presentations before two groups of securities analysts. One meeting was held in New York to better familiarize analysts who follow the Company with Aminoil International, Inc. and Sea-Land Service, Inc. The other presentation took place in Richmond, Virginia, at a tobacco conference organized by Maxwell Associates. The Richmond meeting included a comprehensive presentation on R.J. Reynolds Tobacco Company as well as a review of the performance and prospects of RJR's foods, international tobacco and aluminum products and packaging businesses.

Reynolds Industries

The management committee created by R.J. Reynolds Industries, Inc. last September was a natural step in the evolution of the Company and "reflects the diversified entity R.J. Reynolds has become today," Joseph F. Abely Jr., executive vice president and chief financial officer, told securities analysts at meetings held in New York and Richmond, Virginia, recently.

"This structure is aimed at our most fundamental responsibilities," Abely explained. "That is, ensuring the long-run survival and growth of our Company, establishing the strategic direction and goals to enable this, and bringing about annual results that are both consistent with our strategies and rewarding to our shareholders.

"The management committee ensures that the views of all of the business constituents within the Company are brought to bear on strategic or policy decisions. And it provides a broader base of knowledge across the senior management to provide for an orderly management succession into the future."

Aminoil International

After almost a year of operating the properties acquired from Burmah Oil Company, "we think they were a better buy than originally estimated," Jack Sunderland, chairman and chief executive officer of Aminoil International, Inc., told more than 100 securities analysts at the New York meeting.

"A recent review of the fair market value of the Burmah properties has shown that our pre-acquisition valuation was very conservative," Sunderland told the analysts at the meeting, which was held to better acquaint the investment community with Aminoil and Sea-Land Service, Inc.

Sunderland said that Aminoil's revenues in 1977 should increase to slightly more than $1 billion and that earnings from operations from domestic properties would be "up substantially" from $1.3 million in 1976.

"We are projecting 1977 as primarily a development year for our domestic operations," he said. "However, earnings from operations will be moving up."

In the foreign area, where Aminoil had virtually all its operations until the Burmah purchase, the company expects

(Continued)

(Continued from page 11)

Henry L. Gilbertson

Charles I. Hiltzheimer

Richmond Meeting

to earn continuing profits, the Aminoil executive said.

"Although we plan an ongoing international business, the main future of Aminoil now lies in the United States," Sunderland told the analysts.

Sea-Land Service

Sea-Land Service, Inc. has initiated a program to increase its earnings from operations and "reduce year-to-year earnings volatility while demonstrating orderly growth to the maximum extent possible," Henry L. Gilbertson, Sea-Land president and chief operating officer, told the analysts.

The program includes a redeployment of assets directed at improving the quality of return from the Atlantic service and at taking advantage of new growth opportunities, Gilbertson said.

"Our research pointed up high growth and attractive earnings opportunities in the Middle East, which Sea-Land could serve uniquely with our fully containerized crane vessels," he explained. "We also identified profitable new markets in Latin America."

Mideast service was initiated in late 1976 and expanded early this year.

Referring to the new service, Charles I. Hiltzheimer, Sea-Land chairman and chief executive officer, told the analysts, "Europe-Mideast trade is expanding rapidly. In just nine months of service, Sea-Land carries more containers to Saudi Arabia than any other single company in the world . . .

"During the next several years the Middle East will reflect a growing investment and above-average earnings. Return on assets deployed in the trade is projected to exceed our standards."

Reynolds Tobacco

R.J. Reynolds Tobacco Company has a three-part program to keep earnings growth at healthy annual rates, Wm. D. Hobbs, chairman, told about 50 analysts at the Richmond meeting.

"First, we plan to increase volume and profit through new, innovative, quality products such as Real," he said.

"We clearly understand the dynamics of the tobacco industry and how to capitalize on them. Our new brand success rate and our already high share in the developing low 'tar' category are evidence of this.

"Secondly, RJR has consistently been able to achieve increased productivity.

"Together, new-generation equipment and the expansion of tobacco processes have already saved us close to $42 million and improved our margins by almost two percentage points — and the full potential of these programs has yet to be reached.

"Finally, because of our high volume and efficiencies, we are in an enviable position regarding the pressures of inflationary operating costs. We are able to cover increased operating costs with price increases that are minor to the consumer, thereby maintaining our margins without sacrificing our unit sales and earnings growth."

Reynolds Tobacco expects the environment for cigarette sales over the next five years "to be somewhere between that of the latter '60s and the early '70s," J.H. Sherrill Jr., director of marketing

Wm. D. Hobbs

J. H. Sherrill, Jr.

James R. Peterson

research, told the analysts.

"We do not see any extremes — deep recessions or heavy taxes. Consequently we are forecasting the industry to grow at 1 to 1.5 percent a year — about half the rate of the early '70s, but above the no-growth period of the late '60s."

Tobacco International

Earnings from operations at R.J. Reynolds Tobacco International, Inc. have been helped by the implementation of a value analysis program that resulted in a substantial cost reduction with no sacrifice in product quality, James R. Peterson, executive vice president, told the Richmond meeting.

"The company expects continued improvement in earnings from operations in the 1977-80 period," he said.

"The improved performance reflects a new commitment and a changed direction for the company's efforts in international cigarette markets. The commitment is being backed up with a change in the management philosophy of the company from a sales and manufacturing orientation to a marketing orientation.

"One of the company's major objectives has been to develop a concentrated marketing thrust in every country where it operates. . . . In the past year, Tobacco International has had a number of new product successes, in which the share of market objective was reached or exceeded in each country by year-end."

RJR Archer

RJR Archer, Inc. is aiming to broaden its markets by finding segments where its specialized marketing and technical skills enable it to obtain a competitive advantage, Peterson told the seminar. "Its objective is to operate as a leader in these segments, developing new products and processes that provide advantages to customers. . . .

"One of Archer's key objectives is to provide superior quality products and technical resources to RJR affiliates."

RJR Foods

RJR Foods, Inc. has remained steady in its intention to double its sales and earnings in the next five to seven years, Peterson told the analysts.

"The company intends to do this through internal development and acquisition," the executive vice president explained.

Reynolds has the financial ability to consider many avenues for growth through mergers and acquisitions," Peterson said. "In other words, size within reason is not a constraint.

"We know that this search can be a lengthy and difficult assignment. However, we have not put it on a time schedule.

"Internally, we see ourselves well positioned in two of the three most rapidly growing food store categories — frozen foods and soft drinks. The growth of these categories stems from long-term consumer trends, and we feel they will continue to show premium growth in the years ahead."

In new product development, the company is making "substantial progress," Peterson said.

"We'll have two new products in test market in the second half, and we have more test market introductions scheduled for next year."

RJR Archer hosts 46 scarecrows, 4-H'ers at contest

Three congressmen joined some 300 4-H members at RJR Archer's scarecrow contest, possibly the first such competition ever held. The 46 scarecrows — 23 male and 23 female — were constructed from aluminum materials made by Archer. Clockwise from upper left: Charles Rose, D-N.C.; Stephen Neal, D-N.C.; William C. Wampler, R-Va.

Aminoil part of Mesa discovery

Aminoil USA, Inc. is one of seven participants in South Pelto Block 13 offshore Louisiana, where an oil discovery was reported in July by Mesa Petroleum, operator for the block where Aminoil USA holds a 4.5 percent interest.

The discovery well, 10 miles offshore in 35 feet of water, encountered three pay sands between 12,000 and 13,000 feet with a total of 110 net feet of apparent oil pay.

A six-well drilling platform and a production platform to partially develop the field have been ordered. First production is expected in mid-1978.

Reynolds Tobacco increases prices

R.J. Reynolds Tobacco Company has increased the price of all its domestic cigarette brands and Winchester little cigars by 85 cents per thousand.

The increase brings the price of regular and king-size brands to $14.35 per thousand. The 100mm brands and More (120mm) will sell for $14.85 per thousand.

The new prices represent an increase of about 6 percent. They were prompted by increases in the cost of raw materials, labor and other operating expenses.

Filmco International to make bishrink film

RJR Archer's Filmco International is expanding its facilities in Sedgefield, England, to begin producing biaxially oriented PVC film (which shrinks in two directions) for industrial use.

The $1.5 million expansion will enable the company to compete in the rapidly growing international market for bishrink film in Great Britain and Europe.

RJR Tobacco offers wheelchair blueprints

Handicapped young children around the country can benefit from free blueprints of this specially designed miniature wheelchair now being distributed by R.J. Reynolds Tobacco Company. Young handicapped children can get in and out of the wheelchair without assistance.

Productivity gain aids performance

A 9.5 percent increase in manufacturing productivity figured as a major factor in the improved performance recorded by R.J. Reynolds Tobacco Company during the first half of 1977.

"We have kept pace with our increasing unit sales with no unplanned expenditures for new equipment or facilities," Wm. D. Hobbs, chairman, says. "This is remarkable when you consider the added demands on our production capabilities of a product introduction the magnitude of Real."

Hobbs notes that while production has increased, consumer complaints have decreased in number.

"We keep careful records on the number of letters from smokers about the quality of our products," he says, "and currently the number of complaints is at its lowest level in almost three years."

Aminoil to study 'in situ' extraction

Geokinetics Oil Shale Group — a joint operation of Aminoil USA and Geokinetics, Inc. — has signed an agreement with the Energy Research and Development Administration (ERDA) for development of underground "in situ" (or in-place) methods to extract oil contained in the shale formations found in the western United States.

The project is part of an ERDA program to speed application of several types of in situ processes, as distinguished from processes used above ground to recover oil from shale that has been mined and brought to the surface.

The ERDA-Geokinetics agreement is for the first phase of a four-phase, five-year program, which will cost an estimated $9 million — $5.9 million from ERDA and $3.1 from the Geokinetics Group.

It is estimated that nearly two billion barrels of oil are contained in the western shale formations. Several types of shale exist in the Green River formation, located in Colorado, Wyoming and Utah. The group's in situ project site is in Unitah County, Utah, and its laboratories are in Concord, California. Geokinetics will conduct both laboratory investigation and field development and demonstration at these locations.

Aminoil, 18 others study Cook Inlet

Nineteen oil companies, including Aminoil USA, Inc., are participating in a stratigraphic test well in the Lower Cook Inlet about 43 statute miles southwest of Homer, Alaska.

The well is in an area scheduled for leasing by the federal government in October.

Projected cost of the test well is $11.4 million being shared by the 19 participants. Atlantic Richfield Company is operator.

Six grants awarded

Reynolds Tobacco has awarded six grants totaling $94,875 to five Southeastern universities and the North Carolina Tobacco Foundation for agricultural research related to tobacco.

RJR Foods expanding 64-ounce distribution

RJR Foods, Inc. plans to begin distribution of three additional flavors of Hawaiian Punch in 64-ounce bottles in the entire eastern half of the United States.

Sunshine Orange, Great Grape and Very Berry are now being sold in New York, Washington and Pennsylvania and will be available in all markets east of the Mississippi by the end of September.

Fruit Juicy-Red Hawaiian Punch, the nation's most popular noncarbonated beverage, was introduced nationally in the 64-ounce, resealable bottle in June 1976. In eight months, the product became the fourth-largest-selling fruit drink sold in glass bottles.

With the expansion of the additional flavors, Hawaiian Punch in 64-ounce bottles will be represented in two-thirds of the flavor categories in the glass-bottled fruit-drink market.

Punchy goes to court

Wearing his Punchy T-shirt for good luck, Ricky Leach of Laguna Beach, California, blasts a shot during the USTA Boys' 12 Clay Court National Tennis Championships held recently in Winston-Salem. RJR Foods, Inc. supported the national event. Leach, who placed third in the tournament, was also named the recipient of the Hawaiian Punch Sportsmanship Trophy.

Dividend declared

On July 21 the Board of Directors of R.J. Reynolds Industries, Inc. declared a quarterly dividend of 82 cents a share on the Common Stock of the Company, payable September 6 to shareholders of record August 10.

Aminoil to install production platform

Sufficient additional supplies of natural gas have been found in Aminoil Development's Vermillion Block 325 offshore Louisiana to justify installation of a production platform.

In drilling its seventh well on the block, 125 miles south of Lafayette, Louisiana, in the Gulf of Mexico, Aminoil discovered two new pools of natural gas not encountered in earlier wells. Significant hydrocarbon had been discovered previously in two of the six wells drilled, but not enough to warrant production.

Production will begin as soon as the platform is installed on the lease, and wells and pipeline hookups are completed.

Plant tour features tobacco history

R.J. Reynolds Tobacco Company has revised and enlarged the display included in the tour of its Whitaker Park cigarette manufacturing operations. The display highlights the importance of tobacco in U.S. history and includes a wide selection of tobacco memorabilia. Almost 180,000 persons toured Whitaker Park in 1976.

Two new cigarettes introduced in Brazil

R.J. Reynolds Tabacos do Brasil Ltda. has introduced two new products into test market.

Kingston, a full-flavor, king-size cigarette, is being sold in Sao Paulo.

Chanceller has been introduced into the Rio de Janeiro market. It is a full-flavor, 100mm slim (21mm circumference) cigarette.

RJR
Quarterly Report 2

Second Quarter 1977

Published quarterly by R.J.Reynolds Industries, Inc., Box 2959,Winston-Salem,N.C. 27102

BULK RATE
U.S.POSTAGE
PAID
PERMIT NO. 76
ATLANTA, GA.